[What’s Korea’s “beef” with the US on free trade?](http://welkerswikinomics.com/blog/2008/09/25/whats-koreas-beef-with-the-us-on-trade/)

[Bloomberg.com: Economy – Korea Beef Deal Won’t Yield Trade Vote](http://www.bloomberg.com/apps/news?pid=20601068&sid=aVSG6OYg8UCs&refer=home)  
***Free trade: everyone either loves it or loves to hate it.*** South Korea and the US have been in negotiations for a landmark free trade agreement for years. Korea, however, has had a “beef” with US beef imports since 2003, when a case of Mad Cow Disease gave Korean officials the jitters and all imports were halted.

Even though Mad Cow has disappeared from American beef, the ban has remained, making it difficult for negotiators to come to any major agreements on the reduction of tariffs and other barriers to trade in other markets in which the US and Korea trade. Just last week, South Korea removed the beef ban, giving some analysts hope that a free trade deal may soon be agreed upon.

President Bush signed the agreement last year but has hesitated to pass it on to Congress; where certain Democratic politicians have refused to approve the agreement until S Korea removed the beef ban. Now that the ban has been lifted, however, it appears that the issues keeping an agreement from being reached may run deeper than the simple beef ban:

*In addition, Ford Motor Co., unions and Democrats, including both Hillary Clinton and Barack Obama, all say the accord must be reworked to address what they call South Korea’s barriers to U.S. manufactured goods.*

*“I understand there are foreign policy considerations, but this is too important for us,” Stephen Biegun, vice president for government affairs at Ford said in an interview earlier this month. “We don’t see any sign that they are ready to change.”*

*Levin, who represents autoworkers in suburban Detroit, said the accord will need to be changed to address what he calls South Korea’s* ***non-tariff barriers*** *to U.S. manufactured goods, especially autos.*

*Clinton, in a response to questions from the Pennsylvania Fair Trade Coalition, said the agreement with South Korea “will cost America jobs.”*

The S Korea / US Free Trade Agreement should bring a boost in trade between the two countries:

*The U.S. is South Korea’s second-largest export market behind China, with shipments totaling $45.8 billion in 2007. Imports from the U.S. last year reached $37.2 billion. The trade agreement would eliminate or reduce tariffs on a wide range of goods including automobiles, vegetables and electronics.*

***Through free trade there are winners and losers.*** This is a theme we’ve explored in some depth already during our [International Economics unit](http://welkerswikinomics.wetpaint.com/page/Macroeconomics+Unit+VI+-+Open+Economy%2C+International+Trade+and+Finance). The winners, in the case of the S Korea/US FTA will likely be manufacturers in S Korea and service industries in the US. Judging by Ford Motor Company’s response to the FTA, we can assume that American manufacturers will be losers from the accord.

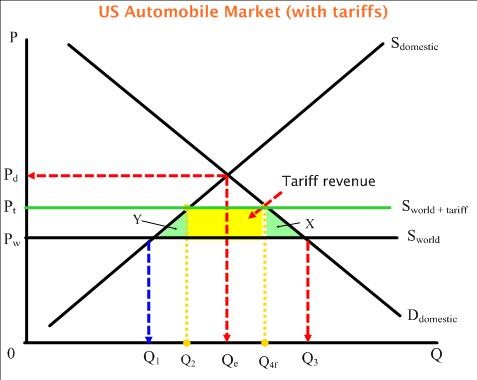
Does this make it bad, however? According to macroeconomic theory, *no*. The removal of tariffs on imports from S Korea will force American manufacturers to become more competitive and achieve greater efficiency, both which will result in a more efficient allocation of resources in both S Korea and the US. If Ford, for example, sells fewer cars because of in influx of high quality, affordable Korean automobiles, then Ford may be forced to shut down some of its plants in the US. This will lead to the loss of American jobs, just as Hillary Clinton claims it will.

But in the long-run, America as a whole should be better off for it. Manufacturers in the US will focus more on capital intensive goods such as industrial equipment, the manufacture of which requires highly skilled labor, which America has in abundance. In addition to industrial equipment and other high skilled manufactured goods, the US service sector should benefit from freer trade with S Korea.

*With beef being resolved, the U.S. banks, insurance companies and other services companies that stand to gain the most from this accord are gearing up their lobbying efforts.*

*Beef “has been our biggest obstacle in having a meaningful dialogue on the benefits of this agreement,” said Matt Niemeyer, vice president for the business insurer ACE Ltd. and a former U.S. trade official. “It’s now time to work with Congress to find a way to move this important agreement this year.”*

As any student of economics knows by now, *politics and economics don’t always mix well*. The opposition to the S Korea/US FTA among Congressional Democrats is more political than it is economic. Jobs will be lost, that’s true, but overall trade between two technologically advanced, developed countries like the US and S Korea should do more for improvements in efficiency and in resource allocation than it will in harm for a handful of American workers who may find themselves out of work due to greater demand for imported automobiles.

  
**\*A tariff on Korean automobiles results in the following outcomes:**

* The quantity demanded of automobiles is less than it would be without a tariff (Q4 rather than Q3)
* The quantity supplied by American auto manufacturers is greater than it would be without the tariff (Q2 rather than Q1)
* The difference between Q2 and Q1 represents an overallocation of resources in America towards automobile manufacturing.
* The domestic quantity demanded exceeds the domestic quantity supplied. The difference (Q4 - Q2) is made up for by imports from S Korea.
* The government earns revenue equal to the area of the yellow rectangle (amount of tariff x number of cars imported)
* Society experiences a loss of efficiency (deadweight loss) equal to the combined areas of the green triangles Y and X. This is consumer surplus lost, accounted for by the higher price paid by American consumers imposed by the tariff.

In the model above, the removal of a tariff on Korean automobiles will result in a decrease in output by American firms from Q2 to Q1, an increase in imports from Q4 – Q2 to Q3 – Q1, and an increase in consumer surplus, efficiency, and better overall allocation of resources in America.

**Discussion questions:**

1. How does the graph illustrate the concept of *“winners and losers from free trade”*?
2. Who gains and who loses from free trade with the US ***within Korea***?
3. Is it possible that a free trade agreement with Korea would actually ***create jobs*** in America? Explain…
4. Why do politicians oppose free trade deals that would result in such improvements in efficiency, allocation of resources, and even in the employment opportunities for American workers?

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[International Trade Made Simple](http://welkerswikinomics.com/blog/2008/08/20/international-trade-made-simple/)

Is international trade really as good for a nation’s standard of living as economists say? And, what the heck is comparative advantage anyway? And what about the foreign currency market and those confusing supply & demand curves? Yes, the quest to understand the economic benefits of international trade is enough to make any citizen or first-year economic student vomit, tremble, get a headache, or at least curse.

Having been an AP Economics’ teacher for 8 years now, I must candidly admit that it took me a few years of study and research to try to reduce international trade to pure simplicity and understanding. Let me give it a shot below. I love simplicity.

The average “Joe Citizen” in almost any country in the world is suspicious of trade, and rightfully so, since he reads or observes factories being closed, jobs lost, and the feeling that somehow his country is going down the toilet as his own home fills up with foreign-made products. Unfortunately, what Joe Citizen does not understand is that the money his own nation is spending for those foreign products (imports) is spent right back into the pockets of his own country, increasing employment and income.

Let’s take a single, real-world, international trade example being careful to accurately explain the whole economic story:

Let’s say that the United States (we’ll say Wal-Mart) decides to buy several shirts costing $400 from a Chinese shirt manufacturer, in lieu of buying those same shirts from a shirt manufacturer in Elon, North Carolina (USA). As a US AP Economics’ teacher I am one of about only 47 Americans in Fairfax County Virginia, which not coincidentally ties to the number of AP Students I taught this year, that quickly understand that the decision to purchase the shirts from China, in lieu of the US manufacturer in North Carolina, is actually BETTER for America and will make my home country better off in the long run! What? Mr. Latter, are you Benedict Arnold, the American traitor, reincarnated?

Let me explain how the US benefits (and China too!) in simple terms ignoring foreign currency transactions, which will just confuse the discussion and cause the student to lose sight of what is really happening:

The first key point is that when Wal-Mart buys the shirts from China for $400 it can only pay China with US dollars. Why? Because Wal-Mart has only US dollars! It has no Chinese currency (Yuan). It literally drains its bank account of US dollars that are transferred/paid to China!

The second key point is that when China receives that same $400 US dollars for the shirts, China cannot, unfortunately, spend any of the $400 in its own economy since only the Yuan is accepted as a medium of exchange in China! China is now forced to either throw the currency away (not advised!), or immediately spend the money back to the USA (advised!).

In summary, China has actually traded a product (shirts!) for paper (US dollars!), and those US dollars cannot be spent in China. For China to receive any value at all for the shirts it sent to America, China must now spend the $400 back into the US economy for, say, a global positioning system (GPS) from FleetMatics out of Waverly, Massachusetts (USA). Cutting through to simplicity, in essence, it’s almost as if Wal-Mart (USA) just paid FleetMatics (USA) $400 directly for the shirts!

Yes, the “punch line” is that all home-currency spending by the domestic nation on foreign products (imports), in turn, are spent right back to the domestic nation increasing the domestic nation’s employment, income, and standard of living. (Note; this is shown in a nation’s balance of payments schedule which always nets to zero, but, yuk, who cares about that right now with summer coming!)

And, yes, let’s not forget that Elon, North Carolina shirt maker that did not get the original $400 from Wal-Mart in our above example! Our nation loves competition (ready for the Olympics?) and I am excited to see if that North Carolina shirt manufacturer can “raise their game” (increase productivity), and hopefully get the next shirt contract from Wal-Mart or some other firm! If not, well, that North Carolina firm may just have to close down.

If you are still reading this post at this point, you may be thinking the following if you have a little economics’ background: “But the US has a growing trade deficit with China, so China may not immediately buy that GPS system from FleetMatics for $400”. And, you are correct, but that is also not a problem for either the United States or China. What China is really doing right now is deciding to temporarily save or invest a minority percentage of their US dollars received back into America in lieu of buying US products. Said another way, China is not buying as many GPS’ as the US is buying shirts and, of course, we call that phenomenon the US trade deficit which immediately seems to speak “problem”. But it is really no problem at all! China is still spending their “saved” US dollars back into the US economy, but in different ways. China is saving and investing some of those US dollars directly into the United States economy by building plants in America, buying US stock to fund American companies’ expansions, and temporarily saving some of their dollars, for future US purchases, by buying US bonds to help the US government pay for the war in Iraq, the war against terrorism, and several other US government initiatives necessitating borrowing. Eventually, China will sell these US bonds and buy that GPS system or build more plants to employ more Americans!

Now one last thing. Promise! Let’s get back to why trade is really so economically advantageous to any nation that pursues it. And by advantageous, I mean how it increases our incomes and standards of living. In one word, the answer is “productivity”. If we go back to the original example of the US buying shirts from China and China taking the US dollars to buy the GPS, we remember that the shirt manufacturer from North Carolina was “left out in the cold” because Wal-Mart did not buy the shirts from them. We can logically conclude that perhaps some Chinese manufacturer of GPS systems was “left out in the cold” because some Chinese business elected to buy from FleetMatics in the USA, and not the Chinese GPS manufacturer. Wow, I love global competition! What a great way to incent businesses in both the USA and China to compete against each other and increase their productivity and conserve our nations’ scarce resources, increase our choice, and lower our costs!

**Discussion Questions:**

1. Which basic economic principles underly the emergence of international trade as a global economic force.
2. Who are the winners and losers of trade between the US and China as explained above?
3. Why do you think free trade is such a controversial topic among certain groups of Americans an other Western nations’ people?